

**REBUTTAL COMMENTS  
OF  
THE ASSOCIATION FOR POSTAL COMMERCE  
THE DIRECT MARKETING ASSOCIATION  
MAIL ORDER ASSOCIATION OF AMERICA  
NATIONAL ASSOCIATION OF PRESORT MAILERS  
NATIONAL POSTAL POLICY COUNCIL  
THE PARCEL SHIPPERS ASSOCIATION  
Before  
THE PRESIDENTIAL COMMISSION ON THE UNITED STATES POSTAL  
SERVICE**

March 13, 2003

The purpose of these comments is to place in perspective several of the assertions contained in the testimony of William Burrus, President of the American Postal workers Union (APWU) and the supporting statement submitted by Kathryn Kobe, of Joel Popkin and Company.

The Executive summary of the APWU testimony begins by taking issue with the widely held view that the 32-year old business and regulatory model under which the United States Postal Service (USPS) operates is in need of change. It “is NOT BROKEN,” and “...is far healthier than many large corporations” claims the APWU. In the context of a triage setting, such conclusions and comparisons would require a physician to ignore vital signs and treat only the terminally ill. Then, a mere two pages into its written submission, the APWU offers a seemingly inconsistent assessment of the outlook in noting that while “not yet broken...[the USPS] does need to apply good business principles.” On this latter point we agree. The USPS does need to apply good business practices. Moreover, to the extent that the

current business model poses an impediment to doing so, it must be changed before the allegedly "not yet broken" USPS is terminal.

The APWU pronouncement that the patient is well relies heavily on the conclusion that mail volume has grown rather than declined. As evidence, it provides a graph, at page 4, depicting the growth in First-Class Mail volume over the past 30 years. Oddly, the very evidence of health--growth in mail volume which is confined almost entirely to the introduction of discounts for worked-shared mail--calls into question other significant aspects of the APWU testimony as relates to work-sharing discounts. In addition, given its reliance on volume growth as the measure of institutional health, we are mystified by the APWU's suggestion that the USPS withdraw from a growth area--the package delivery business.

Any doubts that may remain about the APWU's arguments that the Postal Service is healthy are thoroughly and systematically rebutted in the January 2003 report of the General Accounting Office (GAO) entitled "Major Management Challenges and Program Risks, US Postal Service." Among the many concerns raised by the GAO is "that growth in First Class Mail and Standard Mail has been, on average, declining since the 1980s. Declines in volume growth for these two classes are particularly important because the Service relies on them for approximately three-fourths of its annual revenue." GAO-03-118 at 5.

On the matter of work-sharing discounts, the APWU asserts that they are too large. One section of the APWU testimony is entitled "Gives

Discounts Beyond Costs Saved” and focuses on this allegation. There, APWU asserts, “The Postal Service asks for the ability to give discounts to attract new customers. Yet, it already gives discounts to large mailers equal to about 25 % of the price that individuals and small businesses pay for first class postage. It is especially troubling that these discounts exceed the costs that the Postal Service saves in its systems and that these discounts are for mail that has no alternative delivery service. The current rate setting mechanism forces single piece users to subsidize large mailers and presort bureaus. This causes the Postal Service to lose contribution of each piece that switches to excessively discounted raters. As more mail takes advantage of these excessive discounts and switches to a presort category, this hurts profitability even more.”

The statement is wonderful rhetoric, but it is factually incorrect in numerous important aspects. As is shown below, single piece users do not subsidize large mailers and presort bureaus, the Service does not lose contribution on each piece of workshared mail, discounts for workshared mail do not exceed the costs avoided, and much of the workshared mail does have alternatives. Moreover, absent the introduction of a range of work-sharing incentives for all classes of mail, there is little question but that both the quality of service and financial condition of the USPS would be far worse. In 1999, alone, work-sharing enabled the UPSP to avoid some \$15.3 billion in costs, according to a paper prepared by the staff of the Postal Rate Commission.

## **Work-Shared Mail Does Not Receive a Subsidy**

Testifying in Docket No, R97-1, Dr. John Panzer (USDPS-T-11 at 8) described the test to determine whether a service was being subsidized:

The test accepted by economists to determine whether or not any service (or group of services) is receiving a subsidy is *The Incremental Cost Test*. The revenues collected from any service (or group of services) must be at least as large as the additional (or *incremental*) cost of adding that service (or group of services) to the enterprise's other offerings.

This test is a very intuitive fairness standard. For if a service's revenues do not cover the additional costs the enterprise incurs in providing it, the users of that service are receiving a subsidy from the enterprise's other customers. On the other hand, if the revenues from all services (or groups of services) are at least as large as their incremental costs, then no user or group of users is burdened by their provision. Indeed, in that case, the provision of each service (or group of services) reduces the amount of revenues which must be collected from the remaining services in order for the enterprise to break even. And, the rate schedule is free from cross-subsidy.

The USPS Cost and Revenue Analysis (CRA) for FY 2001 shows that First-Class Presort Letters have an incremental cost of

\$4.966 billion and contribute revenue of \$13.224 billion. In Standard Mail, Enhanced Carrier Route has an incremental cost of \$2.260 billion and contributes revenues of \$4.980 billion and Standard A Regular has an incremental cost of \$8.085 billion and contributes revenues of \$10.630 billion. Thus, under the incremental cost test, there are no subsidies in these large volume sub-classes of mail.

### **Work-Shared Mail Makes the Same Contribution Per Piece as Non-Work Shared Mail**

We do not believe that unit contribution is or ought to be the relevant measure of a “fair” rate schedule nor that an equal markup is the proper measure of whether a discount is appropriate. In any event, the CRA also shows that per piece (unit) contributions are as high for work shared mail as they are for non-workshared mail. The unit contribution for First-Class Presort Letters is \$.179 while it is \$.178 for Single-Piece letters. And while in Standard Mail, there are no single piece mailers and all mail is work-shared to some degree, Enhanced Carrier Route (ECR) mail, which is the most work-shared mail, makes a unit contribution of \$.084 while Regular contributes \$.050 per piece.

### **Discounts in Work-Shared Mail Do Not Generally Exceed USPS Cost-Savings**

Because the In-Office Cost System (IOCS) does not track costs at a rate category level, the Postal Service uses engineering

models to estimate the costs avoided by workshared mail. Discounts are then based on the cost savings. In Standard Mail, it is true that some discounts are more than the costs the models shows the mail avoids, but in other cases, the discounts are substantially less than the avoided costs. And testimony in rate cases has shown that where the discounts are higher than the estimated avoided costs, the Postal Service has underestimated the avoided costs. (Direct Testimony of Sander A. Glick ; PostCom, et. Al.-T-1,R2000-1, pages 9-19.

For First-Class Mail, the FY 2001 CRA shows a marginal unit cost of \$.243 for Single-Piece Letters mail and \$.101 for Presorted Letters. Thus, Presorted letters cost \$.142 less than Single-Piece letters, a cost difference that far exceeds any of the worksharing discounts. Although some of this cost difference may be due to factors other than the worksharing that was specifically measured (see the last section of this statement), the fact remains that the discounts are less, not more, than the cost difference.

### **There are Alternatives to the Postal Service for Some Work Shared Mail**

It is naïve to assert that there are no alternatives for work-shared mail. Standard Mail is advertising mail, and other media compete with the Postal Service for this advertising. Newspaper inserts compete vigorously with Enhanced Carrier Route mail and

newspapers intervene in rate cases to increase the rates for ECR. Standard mailers constantly and increasingly explore the use of other media like the internet and also test the use of smaller advertisements in the mail. As more and more people receive bills, proxy statements, and bank statements on-line, the alternatives to a major portion of mail becomes clearer and clearer. Reducing or eliminating existing worksharing incentives for this mail will necessarily render the electronic alternative increasingly attractive. And finally, the portion of First-Class Mail that is advertising and solicitations, could easily shift to Standard Mail. It is important to understand that a price elasticity of less than one is not the same as no alternatives.

### **Mailers Perform Work, Frequently Mandated, that is not Compensated in Work Sharing Discounts**

It is also important to note that mailers perform a substantial amount of work and thus incur substantial costs that are not reflected in worksharing discounts in order to qualify for these discounts. All mailers who receive discounts must perform list hygiene, periodically checking their mailing lists against USPS-licensed software to ensure that addresses bear correct delivery point barcodes. In contrast, single piece mailers are not required to check the codibility of the address to which they are mailing.

Mailers who receive discounts must also enter their mail at locations determined by the Postal Service and most must spend their own money to

get it to this entry point. And while there are discounts for destination-entered Standard Mail and drop ship discounts for Periodicals, origin-entered Standard Mail and Presorted First-Class Mail must be entered at a location designated by the Postal Service and cannot earn drop ship discounts. In contrast, single piece mailers may enter their mail in a collection box or at a window of their choice. Finally, mailers who receive discounts must prepare their mail for entry in a manner specified by the Postal Service. Work-shared letter shaped mail, for example, must be faced and trayed (with 150 pieces at a minimum generally required for each tray) and the trays labeled according to Postal Service requirements. And there are also requirements for workshared flats. In contrast single piece mailers simply put mail into collection boxes or hand it to window service clerks.